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**PREPARE NOW AND
SURVIVE THE COMING
BEAR MARKET**

This Time Is Not Different



By Mark D. Cook and Michael Sincere

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BEAR MARKET**

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By Mark D. Cook and Michael
Sincere

Foreword by Jack Schwager

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Dedication

by Mark D. Cook

This book is dedicated to my son, Ryan J. Cook, for his inspiration, research, and commitment to the Cook trading rules and principles. Without Ryan's effort, input, and support, this book would not have been possible.

Foreword

by Jack Schwager (author of the bestselling books, *Market Wizards* and *Stock Market Wizards*)

The first time I saw Mark Cook he was a fellow speaker at an industry conference, and he made an impression before he uttered a single word. He came up to the podium dressed in bib overalls. He did this to make a point about his roots, but his choice of dress was not merely show; there was also substance to it. Even though he had made millions trading, at the time, Cook continued to do some farm work himself.

Although it was difficult to justify his manual labor in any economic sense, Cook rationalized his part-time farm work, which was in addition to the fifty to sixty hours per week he put in as a trader, by saying that he was a workaholic. This may have been true enough, but I also believed that Cook would have felt a tinge of guilt if he had worked “only” as a trader while his then eighty-one-year-old father continued to farm full-time.

About a year later (1999), I called Cook to ask him to participate as an interview subject for my third Market Wizards book, *Stock Market Wizards*. He agreed and I flew out to Ohio to meet

him. I interviewed Cook over the course of two days, spending the night as a guest on his farm.

While I was there, Cook took me for a tour of the local area. As we drove along, Cook pointed out various tracts of land, which he identified by a year number. “There’s 1997,” he said, referring to the farm he had bought with his 1997 trading profits. “There’s 1995,” he said a few moments later, and so on. He apparently has had a lot of good years. Cook is almost zealous about converting his trading profits into real assets—and for Cook farmland is the ultimate real asset.

Cook's early attempts at trading were marked by setbacks. Cook didn't just encounter initial failure, he failed repeatedly and spectacularly, losing his entire trading stake several times, and on one occasion, more than his entire net worth. Cook, however, never gave up. Each failure only made him work harder. Finally, after many years of carefully tracking the stock market, filling volumes of market diaries, and assiduously recording and analyzing every trade he made, his trading became consistently profitable.

Once Cook became confident in his trading abilities, he entered several market contests, registering an 89

percent gain in a four-month competition in 1989, and 563 percent and 322 percent returns in back-to-back annual contests beginning in 1992. His annual returns in the subsequent six years (the six years prior to the year I interviewed him) ranged between 30 percent and a stratospheric 1,422 percent. These statistics are based on defining percent return as annual dollar profits divided by beginning year equity, a conservative definition that understates Cook's true performance, because he frequently withdraws profits from his account but never adds funds.

For example, in his low-return year (based on our definition of percent

return), his withdrawals during the year exceeded his starting capital. At the time of our interview, Cook had provided me with his account statements for his most recent four years. During this period, he was profitable on 87 percent of all trading days, with one-third of the months showing only winning days.

I had interviewed Cook only months before the major stock market peak in early 2000. I contacted Cook several years later to get an update before the release of a paperback version of *Stock Market Wizards*. Cook had continued to roll along in his trading. Given his methodology, it makes no difference to him whether stocks are in a bull market

or a bear market.

For comparison, though, during the April 2000 - September 2002 period when the S&P 500 declined by 45 percent and the Nasdaq by 75 percent, Cook's trading account realized a cumulative 114 percent profit compounded (84 percent if measured as cumulative dollars profit divided by the average account equity level).

When Cook contacted me to write the foreword for *Prepare Now and Survive the Coming Bear Market*, he explained he was compelled to write this eBook because of the opportunity he saw developing in the markets. His key

indicator, the Cook Cumulative Tick (CCT) was screaming that a major bear market was imminent. He had seen similar situations three times before: 1987, 2000, and 2008.

In speaking to Cook, I sensed that a key motivation he had for coming out with this book was that this time he wanted to be clearly on the record with his forecast. Cook pulls no punches in his bearish prognostication. Readers will need to decide whether they accept Cook's projection or not, but given his past record, his market views should not be dismissed lightly. For the record, I received Cook's manuscript for review on October 3, 2014 when the December

e-mini S&P contract had closed at 1961. It will be fascinating to see whether Cook's bold call is realized by the ensuing market action.

- This foreword has been adapted from *Stock Market Wizards* by Jack Schwager.

Introduction

by Michael Sincere

I want to thank you for taking the time to read my in-depth interview with Mark D. Cook. He is a recognized stock and options trader who correctly predicted the 1987, 2000, and 2008 market crashes, and also went long in 2009. That is why I interviewed him for this book.

Readers of my weekly blog (www.michaelsincere.com) or my columns at MarketWatch.com have heard my warnings that the stock market has

reached dangerous levels. I grew up watching the stock market and learned to study and analyze it for clues. The market always provides signs of future direction, but you have to know where to look. Mark Cook is someone who knows where to look.

Cook was one of the first to recognize that the stock market was topping out in late 2014 even as the major indices hit all-time highs. He based this conclusion on his decades-long study of the New York Stock Exchange (NYSE) Tick. Using the data he received, he created a proprietary indicator, the Cook Cumulative Tick (CCT).

In this eBook, Cook helps you navigate through the minefields of a bear market. Many investors can profit easily when stocks are soaring, yet are overwhelmed when they continually decline. Bear markets are usually fast and vicious and can crush the unwary trader. Yet Cook has profited more from bear market plunges than bull market rallies, an accomplishment few others can claim.

With his 38 years experience, Cook has not only survived three major bear markets, but has amassed a fortune from them. In fact, he made the most money during these bear markets precisely because they were so fast and vicious.

He will share with you what he has learned as a trader.

Perhaps the most valuable sections of the interview are when he explains in detail the 11 steps of a bear market. By knowing how a bear market unfolds, you will know what to look for to enhance your trading profits and minimize losses. This should be required reading for any trader or investor.

It is also important to remember that the market always has the final word. While most investors hate bear markets, they are a natural part of market cycles. As long as there are stocks, there will be bull markets and bear markets. Today is

no different. We can minimize mistakes by studying past cycles, which is why we created this book.

One last thing: You might wonder why we created an eBook rather than a traditional hardcover or paperback. The reason is simple. The market is changing so fast that we needed to get this information out quickly. We hope you benefit from the results.

Okay, let's get started learning about bear markets from a master – Mark D. Cook.

Michael Sincere

Author: *Understanding Options 2E* (McGraw-Hill), *Understanding Stocks*

2E (McGraw-Hill), *Predict the Next Bull or Bear Market and Win* (Adams Media), *All About Market Indicators* (McGraw-Hill), and *Start Day Trading Now* (Adams Media).

PREPARE NOW AND SURVIVE THE COMING BEAR MARKET

This Time is Not Different

Sincere: Can you give us a brief summary of your background?

Cook: I am Mark D. Cook, a stock and options and futures trader. I'm primarily known for being one of the Market Wizards that was included in Jack Schwager's book. I'm also the winner of the 1992 U.S. Investment Championship with a 563 percent audited annual return.

What do you think investors are thinking right now?

The perception among investors and even traders is that the market only goes up. It will take a major correction for people to change their minds.

Do you see any danger signs?

I believe this stock market has the potential to be the worst of all time. We're very close to a top. I'm waiting for the shot across the bow that signals a crack in the uptrend.

You make it sound like there will be a horrific correction.

There is no doubt in my mind that a massive correction is coming, and it will

be greater than 35 percent. It will surprise everyone, including the masses. I am putting my reputation on the line to say that. When it happens, the devastation will hit quickly. It's like the real estate bubble of 2006 and 2007 where people were super leveraged, and it collapsed. We're also going to see margin calls like you wouldn't believe.

What would be the worst-case scenario?

The worst scenario is a prolonged bear market. I know we're going to have a bear market but I don't know its magnitude. It scares me how bad it will be. Of course we will get the 20 percent correction. I just don't know for sure

how low the market will go. After it hits, we will have a different kind of market. Only the traders will survive. Volatility is the traders' best friend, and we will have a lot of it.

What happens to traders during these low volatility periods?

Because of the six-year bull market and the lack of volatility, many traders I've known have given up and quit. The Fed has chased away the traders. There is no liquidity in the market. It's all one-sided. The problem is that a one-sided market is a double-edged sword. What goes up must come down eventually, and when the market goes down, it will be horrific. There will be no bids. It will

be one-sided on the short side.

I thought people didn't like volatility.

Most people don't, but volatility is a needed component of a free stock market. The public has attached a bad stigma to the word, "volatility," but that is because they are not informed. Volatility does not mean bear market. You need volatility in the market to keep a bull market from getting overzealous. Volatility is needed to correct these distorted markets. Bottom line: Without volatility, you end up with a very dangerous overbought market, ironically, the kind of market that we had in the last quarter of 2014.

What was so surprising about 2014?

In my 38 years of making a living trading, I have seen extreme environments to the bullish and the bearish sides. In 2009, the satanic low of 666 in the S&P 500 will remain in the annals of stock folklore for decades, if not longer. That severe bearish environment destroyed lives, fortunes, companies, and confidence in American business. And now, after five years, we have gone from one extreme to another. As I write this now, many investors believe the stock market is invincible. We have seen these extremes before in many commodity markets, bond markets, real estate markets, and equities. To navigate extreme conditions, I practice

one important rule: Keep It Simple, Stupid! The best market experts I have known are tenacious, patient, and they have kept it simple.

Why are you so sure that there will be a severe correction?

The numbers I'm seeing on my CCT indicator are some of the worst I've seen since 2007 and 2008. A lot of what I'm seeing doesn't make sense. In 2014, we went two years without a correction so the bulls were happy and complacent. They start to think that is the norm. The longer we go without a 10 or 20 percent correction, the greater the next correction will be. Because of leverage, portfolios are going to get hit harder. In

other words, if you get a 20 percent correction, portfolios will go down by 30 percent or more.

What do you mean by the CCT indicator?

The main indicator I use is a proprietary indicator I developed, the Cook Cumulative Tick (CCT). The CCT, more than any other indicator I have used, is reliable, timely, and crucial to understanding the true tape of the stock market. It has paid my bills for over 35 years.

The CCT is derived from the New York Stock Exchange (NYSE) Tick, a leading indicator that gives clues where the market is going to go next. The

NYSE Tick is the heart and soul of the market. It's the true internals of the market structure. If you have a weak structure, the walls collapse under the ceiling.

Basically, the NYSE Tick gave me a snapshot of the breadth of the market at any given time period. Keep in mind that anyone can look up the NYSE Tick. It's available on any chart. But the CCT involves a lot of work. Most people don't want to take the time to write down every one-minute NYSE Tick to calculate the CCT. The reason it's a cumulative tick is that the CCT is the sum total of the minus and plus NYSE Ticks.

How did you first develop the Cook Cumulative Tick (CCT)?

I started doing research on the NYSE Tick in January 1986. The information was easily available from the New York Stock Exchange, which posted the information on its ticker tape (that was before websites). I discovered that the NYSE Tick was not easily understood by the public, or even by most on Wall Street. I put the NYSE Tick on my monitor and watched it daily.

The CCT is an advance indicator of future price movements for the short and long term. When I discovered the CCT in 1986, at first I didn't know what the numbers meant. By 1987, before the crash, I knew exactly what it was telling

me.

What is the difference between the NYSE Tick and your indicator, the CCT?

The only difference is that I count every one of those cumulative bars. If someone is willing to take the time and add up all of the NYSE Ticks, they could do what I'm doing. But you have to look at it over a long time period, not just one day. One day and one week isn't enough to get a reading. It's a months long chart.

Just to give you an idea, on a one-minute chart, there are 390 individual ticks. I record those ticks every day. If you're not willing to do what I do, then you'll have to take what I see at face

value.

How can someone read the NYSE Tick?

The NYSE Tick is a quote that is generated throughout the trading day. First, anyone can view the NYSE Tick on a chart or any platform that has quotes. On many systems, the NYSE Tick symbol is \$TICK, but it may vary depending on the brokerage firm. I look at a 1-minute bar chart. Everyone should have the NYSE Tick displayed on their screen. I believe it's one of the greatest tools ever created, which is why I use the data from the NYSE Tick to create the CCT.

What information does the NYSE Tick give you?

The tick is a speed and horsepower indicator. The greater the speed, the greater the horsepower expended. Therefore, if a large number of individual stocks are printing a price higher than the previous print, the NYSE will register a high *plus* number. Conversely, if a large number of individual stocks print a lower price than the previous print, the NYSE Tick will register a high *minus* number. No other indicator has provided me with more accurate guidance than the NYSE Tick. It gives an accurate, precise, and an incredibly helpful insight into the internals of the market.

In a normal market environment, when you have an uptrend, you will have a plus tick. The greater the stock prices, the greater the plus tick. If you have a huge uptrend day, which I consider to be 1 percent or greater, you will see a lot of instances of a prolonged plus tick. In an ordinary environment, when the market is rallying for a long time period, the NYSE Tick accelerates and expands in conjunction with stock prices. Simply put, a plus tick equals plus stock prices.

If there is a huge uptrend day, you might see a reading of plus (+) 1000 or greater. Therefore, if the NYSE Tick is registering a plus 1000 or greater, at that particular instance, there are 1000 stocks printing a higher price than they

did previously on the last executed print. It's just the opposite when the tick is minus 1000 or greater.

By the way, those plus 1000 days are rare but meaningful. It's like the accelerator is pressed to the floor and the horsepower and acceleration make the prices go faster. The greater the number of ticks recorded, the more the S&P 500 will advance. Conversely, the greater the number of minus ticks, the greater the fall in the S&P 500 index.

When did you realize the NYSE Tick could help you trade?

I got my Eureka moment in 1987 when the NYSE Tick started registering *minus* NYSE Tick readings while the market

was going up. I realized the NYSE Tick was giving a warning sign, similar to the red line on a tachometer gauge. This meant the engine was warning that going this fast could destroy the engine. In other words, the stock market was moving up so high that the internals of the market could get destroyed, and there could be a crash. I was getting extreme readings over 1000.

So readings over 1000 are extreme?

Yes. It occurs less than 3 percent of the time. The other 97 percent of the time, the NYSE Tick falls within a normal environment. When I see a reading of plus or minus 1100 or 1200, that is even more rare, perhaps one 10th

of a percent. The main point is if the market is going up this high, there should be a plus 1000 tick. When there are movements up, it should correspond.

So the tick was giving negative numbers while the market was going up?

I wouldn't say negative. You should not get a less positive reading when you have a positive price movement. They should go hand in hand. And guess what? That is what I am seeing right now. The market internals don't have the horsepower to keep going higher. As soon as we get a bad news item, or something unexpected, the market will go down. The horsepower is getting

weaker. The market is going higher on fumes. Pretty soon it's going to just quit, and go backwards. The market is inching its way up but there is no horsepower. We're not registering plus thousand ticks. When the market goes down, you will see extensive ticks on the downside. The prices are going up but the tick is not following. It will eventually go in the other direction. The steeper the hill, the faster it will go in the other direction.

How bad could it get?

If the NYSE Tick ever makes it to minus 1600, a rare reading, the stock market engine could blow. The term that engine experts use is "dieseling," where

the RPM escalates in an overheated environment. Put another way, the engine becomes a missile, i.e. it blows a gasket. This is the point I call the “uncle point,” where the pain will be so great someone cries, “Uncle!” To put it into perspective, in 2009, the tick reading was minus 1600, a very rare event.

The intensity of the selling that we are going to witness will be like nothing we have experienced before. In 1987, there was a reading of minus 2000, which is when you will get a crash. It was down 20 percent in one day.

So the NYSE Tick doesn't always go in tandem with stock prices?

Exactly. In fact, the fascinating part is

when stock prices move up but the NYSE Tick does not. It is divergence. The greater the divergence, the bigger the market will reverse direction in the future. To put it into perspective, in the winter of 2014, I was consistently getting less positive readings as the stock market prices held. That is very rare because eventually stock prices have to catch up with the NYSE Tick.

What is the NYSE Tick showing you now?

I have never seen these extreme readings in 28 years of studying the NYSE Tick. That's why I have been warning people. According to the tick, we're already in a bear market but the

prices haven't confirmed it yet. Right now, there is a higher probability of us going down 20 percent than up 10 percent.

In 2008, the divergence between the CCT and stock prices was even worse than in 1987. And now, in 2015, it is worse than 2007. There are fewer and fewer stocks moving up. The weaker stocks in the S&P 500 are getting weaker, and even medium stocks are turning negative. The tape looks terrible to me but it still doesn't fall. It's remarkable, but it won't last.

Recently, the S&P has moved with less speed and less horsepower. The NYSE Tick is registering more minus numbers while stock prices are going

sideways, which is another divergence. It's similar to taking a bus up a hill that doesn't have enough horsepower to make it to the top. This is what could happen to the stock market. There's not enough power to sustain the climb.

Could the NYSE Tick be wrong?

To my knowledge, the NYSE Tick has never been wrong. Eventually prices must catch up with the tick. As prices go up and there are fewer new highs, it's a sign the market is losing energy. I believe that when the smoke is cleared, the coming bear market will exceed 53 percent. In 2014, some might have wanted to put me in a straight jacket. By the end of 2015, I think there will be a

major correction. Truthfully, it scares me to death.

Why does it scare you?

Towards the end of 2014, stock prices kept moving higher but the NYSE Tick kept weakening. The rallies in prices were not accompanied by plus 1000 ticks. On many days, prices advanced while the daily CCT registered a minus number. This is a rupturing of the guts of the market.

Why is there such a huge divergence?

I believe it's the Fed. I'm a tape reader and I watch what is happening in the S&P 500. What I am seeing can only

happen with a monstrous computer program. This program often comes in at the last hour to try and save it. Even with all this money, the S&P didn't have a sustained rally. This time the damage is going to be worse than in 2007.

My indicator is telling me that the computer algorithms that are manipulating the market cannot handle it if we get a huge down day, such as down 200 on the S&P. It will tear the machines apart. There will be no buying when that happens. This is happening because the Fed has created a bubble of bubbles. I have never seen it so skewed. It's a textbook bear market condition.

For example, in September 2014 the Dow was making all time highs while

the Russell was down 10 percent. This is classic bear market behavior. The old adage is the Dow is always the last index to reach an all-time high before there is a major top. Right now, the NYSE Tick is screaming, “Get out of Dodge!”

Could this divergence between prices and the NYSE Tick go on indefinitely?

No. Not indefinitely. But the extension of time will create an even greater divergence that has to be snapped back together. In the previous three instances, 1987, 2000, and 2008, the market crashed by over 20 percent within months of the reading. Usually, you have

three months leeway before the market falls. With the September 2014 reading, I can't say when the market will fall, except that I know it will, and it will be horrific. An engine not utilizing all cylinders has diminished horsepower. A market with a diminishing NYSE Tick has diminished internal power.

Is it possible you're just seeing a strong bull market?

Not now. As the NYSE Tick expands, develops, and matures, it will eventually get overbought. Prices will still go up along with the NYSE Tick. That's ordinarily how a market develops a top where it is plain overbought and due for a short-term pullback. That is how a

normal market operates. However, if I get a lot of minus ticks, prices also decline. The market is a pendulum, and that's how it's always worked.

But, and this is huge, there have been three instances in the past when stock prices and the NYSE Tick have diverged radically. In these rare instances, prices will be still going up but the NYSE Tick is showing less positive readings. The three other times this occurred was in the summer of 1987, the first quarter of 2000, and the third quarter of 2008. Each was followed by a severe market crash.

The fourth time I have seen this reading began in mid-April 2014. The market has been deteriorating since then,

but it's taken a long time for prices to retreat. Actually, during a typical bear market, the last piece to fall is the price. Many people don't realize that.

What was the worst market environment you remember?

I wasn't actively trading in 1973 to 1976 but it was a terrible market. That was during the Nixon Watergate trial. We went from 1000 on the Dow to 600. Brokers came into work and asked, "How far will it go down today?" Every day the market went down. Every day! After Nixon resigned, no one wanted to be in the stock market for a long time.

As for me, the worst market environment that I experienced was the

1987 crash. Thanks to the NYSE Tick, I had my first million-dollar profit in 1987, but after the crash, stocks were hated. The only ones who survived were short-term traders. The fear I have now is that we could go through another 1987 type crash.

What do you remember most about 1987?

I remember what happened before the crash. I was working for a firm called E.F. Hutton, one of the top brokerage firms in the country. They were the company with a popular advertisement that said, “When E.F. Hutton talks, people listen.”

In July, the company took 250 of its

top brokers to Manhattan as a reward. They showed us their new building, a glass tower that was the most opulent thing you ever saw. It had a four-story foyer. A few of the brokers joked that this must be the top of the market. It turned out they were right. Think about this: In July 1987, E.F. Hutton was one of the best in the industry. By October, there was no more E.F. Hutton! They went from King of the Hill to a name found in the history books.

During the next bear market, other brokerage firms will also suffer immensely. When there is no volatility, commissions will die, there will be no trades and few opportunities. Even now, I'm sure the trading rooms in New York

and Chicago are screaming for volatility. That will change as soon as the bear market starts and volatility is returned to the market.

What did you see before the 1987 crash?

There was total complacency. No matter how bad things got, no one thought there would be a 20 percent correction. Not only did it correct but it fell by 20 percent in one day. No one believed the market would go down by that much. That period spawned the term, “Black Monday,” the day of the 20 percent correction. Computers could not keep up while orders were executed in a pricing black hole.

Were there warning signs before the 1987 crash?

Yes, there were, and in hindsight everyone saw them. First, the 1987 market was standing on a very weak foundation. The stock market is similar to a large skyscraper that requires a solid foundation to withstand volatility and adversity. The 1987 environment was a tranquil, peaceful bull market that buyers universally thought was safe. The economy had been in an upswing for several quarters since the previous Fed chief, Paul Volcker, had contained the evil monster, inflation.

The market had been making steady progress since the great bull market had begun in August 1982. At that time, the

Dow had crossed the 1000 threshold and had never looked back. Between 1982 and 1987, there were bumps but nothing of great significance. Any decline was met by rallies that spread through all sectors of the market. The breadth expanded, as did volume, and many stocks made all-time highs. The attitude among investors was that buying on the dip was safe and prudent. Chartists became cheerleaders for the bull market as the chart showed a massive uptrend. What could go wrong?

What else do you remember during that time?

Fear was minimal, and 1987 began with the hope of economic prosperity.

The Fed had a new chieftain, Alan Greenspan. The changing of the guard from Fed Chairman Volcker to the inexperienced Greenspan was noticeable. New Fed chiefs try and establish themselves and cut their ties to the previous chief by taking the economy in a new direction. Greenspan was developing his own agenda that was distinctly different from Volcker's.

Volcker, the old and experienced veteran, had successfully navigated the market through a dangerous storm, and successfully beat back the enemy, inflation. Investors were complacent because they believed the market was unstoppable. As the market continued to rally, making all-time highs, it totally

erased any fears of a bear market, or even a significant correction.

The most noticeable difference was the call option premium valuations, which was a precursor to the widely watched volatility index, or VIX. In 1987, there was no VIX. Nevertheless, call options were incredibly cheap because volatility was so low. When options are incredibly cheap, that's a red flag. Ironically, that is what we saw in December 2014. Everything is contracting: volatility, volume, price movement, and speed.

What did the NYSE Tick tell you back then?

When I looked at the NYSE Tick in

1987, I saw alarming numbers. The internals were showing a crash but the prices were not. I noticed that the rallies were very anemic. The high stock prices had covered up all the cracks so most people didn't see it. It was like a 90-year old running a race at full speed. By the third week of August 1987, we were at all-time highs. In September 1987, many pros wondered what was wrong with the market. The market internals were crumbling while the market labored to go up.

Put another way, the market breadth is when many stocks and sectors are going up at the same time. But if some sectors are going up while others are going down, that is the cracking of the dam. In

1987, the breadth of the market was terrible. When you have no volume or volatility, then the breadth is weak. For a bull market to continue, you need volume. However, before prices retreat, breadth begins to weaken. Many people don't see this, but day-to-day tape readers like me see a glaring red flag. The institutions were not willing to commit money in any sizable amounts. This was indicated by fewer and fewer plus 1000 tick readings.

Before the 1987 crash, the NYSE Tick showed diminishing energy. It was acting like an old engine that had lost power. All the cylinders were not firing properly, like a missing spark plug, so horsepower was minimized. We were

slipping into negative territory.

When was the 1987 top made?

The actual numerical top was made in August 1987. This translates to a triple move in the Dow in only five years. The triple valuation is important to remember. During that time, in 1987, there were many changes. A new Fed chief was appointed, inflation was driving people to despair, and gas had just crossed a dollar a gallon for the first time ever. However, interest rates were rising, which rewarded savers. This is completely different from what is happening in 2015 when the Fed's policies have discouraged saving.

Does 2015 remind you of 1987?

When I think of the similarities between now and 1987, it's remarkable. In 1987, there was an increase in complacency, greed, and increased consumer consumption. A popular movie at the time, *Wall Street*, had a mantra: "Greed is good."

From late August until mid-October 1987, the stock market went through a dark period. It resembled a storm that was a gray spot in the horizon. The perception among investors was it will be a sprinkle, not a tornado. Remember this was also the honeymoon period of Fed Chairman Alan Greenspan, so more latitude was given to him without proper scrutiny. By his fifth month, he had to

handle the biggest crisis since the 1929 crash.

Janet Yellen is the new Fed chief, and she is still learning the ropes. Just like in 1987, there is complacency, greed, and increased consumer consumption. History does repeat itself.

Why did you think the market was going to crash in 1987?

In September, the market slipped a little, and it seemed sluggish. The heaviness of the tape reminded me of a bus trying to get to the top of the hill. The heaviness of the tape told me the bus was overloaded and no one was willing to disembark. Several times, the upward moves in September were painstakingly

slow or stalled.

The NYSE Tick was giving a warning that there was no energy. The bus was overloaded with bulls and it crawled higher but on little gas or horsepower. The last bulls climbed aboard an exhausted, powerless bus with poor brakes. The hill was too steep, the load was too heavy, and there was too little horsepower and inadequate brakes. Looking back, there were red flags everywhere. The bulls did not know they were doomed. The bus careened backward over a steep mountain.

What happened when the market crashed?

The earthquake hit on October 29,

1987: Black Monday. That morning, there were no bids. I'd never seen anything like that in my life. When it rolled over, it was like an avalanche, and we had a 20 percent crash in one day. This was a short-lived bear market. After six weeks, the market lost 35 percent. It was incredible the amount of money that was lost. That wave pushed the 90-year-old over and the crash occurred.

The reason for the crash is unknown, but the fallout was devastating. We went from an all-time high to a massacre. My theory is that when a market gets that high, it gives back everything. In six weeks, we gave back 18 months of gains. It was horrific. After the crash,

they blamed computerized trading for the crash, so they made a new rule: no computerized trading. Obviously, that rule didn't stick. And now, 20 years later, we've gone full circle. If there is a crash, they'll probably blame it on the high-frequency traders.

Before the crash, at first I wasn't even sure what the NYSE Tick was telling me. Fortunately for me, I figured it out in time. I had seven accounts loaded with put options. On Wednesday, I paid \$4 for the puts. On Friday, they were worth \$11. By the end of the day of Black Monday the day of the crash, they were worth \$128 each. From \$4 to \$128. Incredible.

What did you learn?

1987 was an abrupt awakening to reality. All-time highs were hit in the S&P 500 after a very persistent bull rally carried prices higher and higher. It worried few and fertilized greed in many. If you look at a chart in 1986, you'd see a progression of higher highs. In 1986, confidence was growing. Complacency turned into greed at the beginning of 1987 until the October crash, which wiped out the prior 18 months of gains in six weeks.

Is this the fate of the 2015 stock market?

If I overlay the 1986 and 1987 chart on 2015, it's possible the 2013 and 2014

gains made by the S&P 500 would disappear. In my opinion, there is a good possibility we will see a 20 or 30 percent correction in 2015. It could get even worse because complacent investors will buy on the dip. Eventually, greed turns to fear and a lower low could be reached. The next decline will be the proverbial bear market. That's when the bear has clawed a gash on the bull that will bleed the bull to weakness. I will look for four times average volume and capitulation. Because bear markets are hard to time, you try and look at the bigger picture. I stay away from making specific predictions because so many bad things can happen. When we get there, there

will be ways to make money.

Could it really get that bad?

Yes. The second wave down will pass the first support area and continue trekking downward. With each downward thrust, volume will gradually increase at an alarming pace. It will take a considerable length of time for complacent investors to change their mindset to terrifying fear that marks true bottoms. Much carnage must take place to stock prices before there is real fear. Also, each bounce must lack conviction with diminishing volume. All rallies will appear as if they are a person with tennis shoes trying to walk along an icy sidewalk.

So you really think 1987 could happen again?

Absolutely. The 2014 market is eerily similar to 1987. I see the same complacent attitude. The market edged up in 1987 but it felt like you were building a house on sand. In 1987, at first I didn't know the NYSE Tick was screaming Red Alert. The longer the warning signal persists, the greater the correction will be. A failure to address the problem will tempt fate. There were three major bubbles in U.S. history: 1987, 2000, and 2008. I can add one more to the list: 2015.

What other similarities do you see with 1987?

In 1987, a few days before the crash, the NYSE Tick was busting apart. And then, on Black Monday, there was a 20 percent decline in the S&P in one day. I thought I'd never see numbers like that on the NYSE Tick again, or on my CCT, but I'm seeing them again. The foundation of the building is weakening and is turning into dry rot. If you look at the outside, you don't see it.

I'm nervous right now because the NYSE Tick is in a bear mode and headed south. The NYSE Tick always precedes prices, and this has been happening for months.

What else did you learn during this period?

In retrospect, the more complacent the investing crowd is, the greater the danger. In 1987, interest rates were much higher than in 2014, but they were still considered benign. This led to another danger sign, greed. People were borrowing to purchase stocks and bonds, and it grew at an alarming rate. It became acceptable to borrow money from various sources including your broker. After all, fear was obliterated by greed.

In 1987, bullish mutual funds were attracting large sums of money as the Dow crossed 2,700, more than triple from the start of the 1982 bull market. Few investors had a fear of heights. Brokerage firms pounded the bullish

drums. At E.F. Hutton, they unveiled a four-story lobby that I thought was a total waste of money. High-level officers, who saw no danger in the lofty heights of the market, had spent too much money. Greed prevailed on Wall Street.

How about the crash of 2000 to 2003? Any similarities?

Yes. In 2000, every rally got worse and worse, and by the time we got to 2001, the NYSE Tick was negative, which means the cumulative number on my CCT was also negative. I used to get phone calls from desperate traders, "Save my portfolio!" I told them the horse was already out of the barn. Even old time bulls got their clocks cleaned,

and their portfolios were bleeding. Many people I knew did not survive 2000 to 2003.

Do you also look at the bond markets for clues?

Yes, I study it every day. In 1987, the bond market started tanking, leading the stock market by three or four months. That drove the stock market down. In the summer of 2014, the bond market topped out 18 months earlier. The lead-time is usually not very long, and that's what scares me. We could be entering the longest bear market I've ever known.

Another thing I see right now is that bonds and stocks are out of synch and disjointed. Stocks and bonds are usually

wound together, as if they are in love. Now, stocks and bonds are acting as if they're not paying attention to each other, and that doesn't make sense. They are barely communicating. The divergence between stocks and bonds is not healthy.

My greatest nightmare is what happened in the early 1970s when the market goes dead and there are no opportunities. For years after the 1970s, the market went absolutely nowhere. Only traders survive when that happens. All you can do is trade swings because there was nothing else to do. In those days, Ma and Pa avoided stocks, but they would buy mutual funds. Few people wanted to hear about the stock market. Right now, you have to know

how to make hay when the sun is shining because a storm is coming.

I can't prove it but I wonder if the Fed is using all its energy to keep the stock market up. Maybe Fed Chief Janet Yellen believes the stock market is the key to her success. She has little understanding of the stock market, or what to do if the market gets out of her control. It will get away from her. What will be the trigger point? I have no idea, but think of a vacant building that has a gas leak. The gas has been leaking for a long time. The longer the gas leaks, the bigger the explosion. It will take a catalyst to trigger an explosion, but no one knows what that catalyst will be. The longer the gas is in there and

ignored, and forgotten, the greater the explosion. The stock market is like the vacant building. Something major is going to happen that will be massive. It's not tomorrow, but it will be something that creeps up on you like the leaking gas. When it blows, the explosion will be horrific. What will be the trigger point? I don't know.

I see you're not a big fan of the Federal Reserve.

No, I'm not. The Fed has helped to create one of the biggest bubbles in stock market history but they don't see it, or they're ignoring it. They can't ignore it forever. You have to be a student of the stock market to understand this. I believe

the Fed thinks that all you need is low interest rates for a strong stock market. So they will do everything in their power to keep interest rates low. They just don't get it. After all, interest rates are higher than two years ago and the market still went up.

I don't think Janet Yellen understands the stock market, but she's not the only one. The Fed has a long record of not recognizing bubbles. Alan Greenspan didn't see a bubble, nor did Ben Bernanke, nor did Janet Yellen.

So every Fed chair has problems?

If you go back in history, every Fed chairperson, going back 40 years, within the first year, there are cataclysmic

economic fiascos that plays out in the stock market. Volatility increases and the VIX often goes into the 20s and 30s. And because they are new, they don't know how to handle it. In October 1987, within a year of Greenspan's being Fed chairman, we had a crash. And when Bernanke came in, within a year, we had another major collapse. They put the new chairman in without experience, and they don't know what's going on. And now Janet Yellen is the new Fed chairman.

So you think the Fed will mishandle the market?

I'm convinced it will be even worse on the downside than I imagined. The

market is so ripe for a collapse. Yellen doesn't have the speed, dexterity, or experience to manage a collapse when it occurs. The story is always the same with the Fed. I've seen it so many times.

I think the market has gotten away from them. In fifteen straight months, they poured over a trillion dollars into the bond market. No one asks them how they are going to unwind all of this debt and start selling it. It makes no sense to me. They are going to have problems unwinding their programs.

To me, the Fed is like a guy who owns a fast sports car that he can't control. He keeps going faster and faster until it crashes. Eventually, people are going to realize that the Fed is all smoke and

mirrors. After the market plunges, they will come out with a new plan and the market will grasp at anything that gives them hope. The next time, it will be like Chicken Little, and people will stop paying attention to them. They will lose all credibility.

But they listen to them now, don't they?

The Fed makes us feel good and gives us the false hope that the stock market is fine. But when the market unravels, it will be like a person you trust who is beyond reproach, but who is lying to you everyday. When you find out your friend is lying, you lose all trust. That will happen to the Fed.

Everyone thinks the Fed controls everything and will bail everyone out when the market starts to correct. Even the Fed thinks it's invincible. Throughout its history, the Fed is notorious for always being slow to react. I have no idea how they are going to extricate themselves from their current position.

What should they do?

That ship has already sailed. It is too late. If they reduced the excessive amount of money printing, and had some parameters, the damage wouldn't be so great. If they had allowed a 20 percent correction, and not allowed the market to get so high, they could have minimized the damage. The last

quantitative easing was like going 125 miles an hour and then accelerating to 150 miles an hour since nothing bad happened.

The Fed got too big for their britches. They think they are invincible, but they're not. In the past, when things unraveled and there was a crash, they would divert blame to an outside force. No one took responsibility. I see the Fed as being in a pitch-black room wielding a sword. They are swinging the sword around without knowing who is in the room. After the sword kills someone, they panic. They have a powerful weapon but don't know how to use it.

Should investors be aware of what

the Fed is doing?

Yes. For example, you should always know when the Federal Reserve has its FOMC meeting. This meeting is a game changer. Unaware of what the Fed is doing is similar to walking down the stairs in the dark.

Do you think the Fed is afraid of inflation?

Yes. If they acknowledge inflation, they will have to raise interest rates. The Fed is afraid of that first raise. When they do raise interest rates, they will probably raise it a quarter, which is nothing when it comes from zero.

There is nothing more grievous than inflation. It's a heinous monster that can

damage the U.S. economy. So what does the Fed say? They said they want to bring inflation higher. They act like it's not very bad. What is going to happen is inflation will get away from them like it did in the late 1970s.

Paul Volker, the Fed chair in the late 1970s, hated inflation. He attacked it by raising interest rates to 21 percent on short-term money. I personally purchased Certificate of Deposits with a 21 percent annual rate of interest. Twenty-one percent! Today, that's unimaginable. Volker thought inflation was an infectious disease that ruined prosperity, and he let everyone know. He said it was our enemy.

In 2014, the Fed said that it wanted

inflation, and acts like we need more of it. I'm sure that Volker is shaking his head at those comments. Inflation is not something the economy wants or needs. By the time the Fed realizes that inflation is our enemy, it will be too late.

I don't think the Fed has a handle on inflation. One day it is going to boomerang back at them. The Fed does not want to hear about inflation, and they almost don't acknowledge it at all. They keep denying that it exists.

Can the Fed keep saying there is no inflation?

The credibility of the current Fed will erode quickly if they act like there is no inflation. People will start by

complaining about the grocery bill and taxes. As general living expenses go higher, no one will believe the Fed if they say inflation is at 2 percent. Eventually, the Fed will have to raise interest rates to counteract inflation, but by then they will be behind the curve.

What do you think will happen to the market in 2015?

I can't say when it will happen, but I wouldn't be surprised if 2015 will be the beginning of a bear market. There will be numbers on the NYSE Tick that I've never seen before. I can't say there will be a crash, but I can clearly see the signs there will be a 20 percent or greater correction in 2015. When it

starts initially, it will limp along, and the rallies will have less energy. You need to see lower highs and lower lows in the major indices, similar to a declining stair step. It could take months and months. Every rally aborts before the previous high, and every decline penetrates and accelerates to a lower low. That's when you know the correction has started.

Can you give an example of a rally that has less energy?

In March and April 2000, the market made a higher high, which caused euphoria among many investors. I never saw anything like it. However, by the end of April, the market broke to the

downside and the rally crumbled. I'm seeing the same thing now. In December 2014, prices made a higher high in a very short time frame. I will not be surprised to see this rally run out of steam in early 2015.

What's so important about rallies?

You can tell the strength of a market by the way it rallies rather than the way it declines. Most people look at the downturns, but I get my clues from the rallies. If the rallies are sluggish and heavy, that is a clue the market is close to rolling over. It's the next rally that will set up the next calamity. In a typical bear market, all of the rallies are very tepid. People get excited when there is a

decline, but I look at how difficult it is for a market to rally, or to get back to its old highs.

Do you believe the S&P is in a bubble?

Yes. Few people say the market is in a bubble. It's a heinous word to investors. Right now we're in the denial stage. Everyone, including the Fed, denies there is a bubble. If the Fed had backed off and let the market go down naturally rather than trying to talk it up, then they could have prevented a bubble. But for some reason the Fed doesn't want the market to go down. That is unnatural and unhealthy. The Fed hasn't learned anything from the 2008 and 2009

debacle. They still give everyone false hope.

What do you tell people who think you're exaggerating how bad it could get?

In 2000, no one remembered what had happened in 1987. When I gave speeches, I could have been talking in a foreign language. We're seeing the same thing now. I just can't believe that memories are so short. A person who does not diligently study the consequences of past history is doomed to repeat those consequences, and face the future unprepared.

I was one of the speakers at a day trading seminar in February 2000, and I

was almost laughed off the stage. No one would listen to me when I said the market would correct by 50 percent. They didn't want to hear my warnings. They did want to hear from the main speaker who actually proclaimed, "It's different this time," and the audience ate it up. I was thinking to myself, "What a moron. It's never different this time." Not surprisingly, they never invited me to speak at the conference again.

Only a few months later, the market crashed. And now, there's a whole new generation of investors ready to get slaughtered. When the market goes south, you will not find a rose among any thorns. The devastation will be widespread.

So what do you believe will happen in 2015?

Right now, there is no foundation under this market. I'm amazed that the market still hasn't had a 10 percent correction in over two years. That is very unusual, and it tells me the correction will be even worse than in other bear markets. If that isn't a bubble, I don't know what is.

The NYSE Tick and my CCT is showing we're already in a bear market. I saw this in 2000 and in 2007. It's like being in the Twilight Zone. It's similar to going outside on a rainy day and getting sunburn. It's totally abnormal. It's ripping apart the inside of the market. It's like having small cracks on a dam,

cracks that are imperceptible to the eye. Finally, the dam gives way. Eventually, prices will go south and the NYSE Tick will be even worse than I've ever seen. Also, the longer the duration, the greater the move will be.

If we're already in a bear market, why does the market keep going up?

I believe we're in a bear market but prices haven't confirmed it yet. The prices are always the last indicator to confirm a bear market. The public believes the first indicator is prices, but it's the last. We are waiting for price confirmation. In a bear market, the market gets heavier. The market is entering into a terminal stage. The longer

it goes without healing, the greater the injury.

It almost sounds like you want the market to crash.

No, I am not excited about a crash. In fact, a monster crash is not good for anyone. I'd rather have a correction than a crash. Once there is a correction, it increases volatility, which is when I make the most money. After a major crash, there are few opportunities to trade. You either have to be all in on the short side or you miss it.

Remember this: The first break of the market is short-lived and dynamic. That is what we had in mid-October 2014. If there is a correction, instead of being

short-lived, it could take several months or years to hit bottom. There will be many trading opportunities on the way down. I hope it's only a correction and that volatility returns to the market.

How do you define a correction?

A 10 percent correction is a normal event that occurs periodically. A 20 percent correction is similar to an obese diet. The correction that is coming for 2015 - 2016 will alter complacent attitudes. The complacency has stretched far longer than anyone imagined, thanks primarily because of the Fed's easy money policies. A 30 percent crash is the cold turkey, no-more-Twinkies diet that is prescribed for the perpetually

plump bull.

What would a severe correction be like?

It could be like 1987: Short and sharp with high volume, a devastating knife blow. It could also be a long, drawn-out affair, which is what I think will happen. I think a 20 percent correction is a high probability, and any rally would be tepid.

In this scenario, the bounces are anemic, and give little satisfaction to the buy on the dippers. In fact, nearly every buy on the dipper goes underwater over a torturous time period until they can't stand it anymore. The market attracts buyers on the way down because they

see it as a great opportunity to make money. But the market goes down farther than anyone can imagine. It would be nothing to lose 400 to 500 S&P points. It could take us back to 1500 or 1600 on the S&P, which is a 20 percent correction. There is also a growing probability that a greater than 30 percent correction will be seen from the all-time highs to the bottom.

Many long-term investors will sit on their hands and stay in the market. They are told not to worry, be happy, that it's a buying opportunity. Meanwhile, the market keeps falling. This could take years to play out.

When there is a major market correction, many people will not go in

the stock market again, especially anyone near retirement. They will not risk their retirement money. Fund managers will be hated, despised, and avoided. Many mutual funds will close as investors flee.

What is the catalyst that can cause this kind of correction?

No one knows where the catalyst comes from. I think the ship is already taking on water, even though the prices don't reflect that. The cannonball that will finally sink it will come from a source that we don't see. But when the cannonball hits a ship that is already partially flooded, it sinks a lot faster. I'm not sure the Fed is quick enough or

flexible enough to head off a disaster.

A multitude of things that can happen but I don't know the trigger. It can be an external influence such as a Fed statement, economic report, war drums, political statement, or news announcement. The numbers I'm seeing on the NYSE Tick tells me that something could come out of left field that will create a strain on the market.

Virtually every major top has to have a blow-off. In October 2014, we had an approximately 10 percent correction in those indexes in less than a month. But then they reversed. The bounce from the 10 percent correction in the indices was very tepid. The volume was lower and the NYSE chart grew weaker. Because

my CCT did not rally as high as before, it was a divergence. A divergence of a lower CCT with higher prices creates downward pressure.

What should traders do if there is a correction?

If you are short, cover your position after the first correction. Then stay on the sidelines as the market rallies, then short on the next upswing. This is for traders only, not investors. If there is an extreme day, I might take half my position, or sell it all depending on how extreme. The sharp first break in the market usually doesn't last long, and it rallies back. After the S&P falls by 10 percent, people will buy on the dip.

When the subsequent rally stalls out, that's when you better watch out.

How will you know we're in a dangerous environment?

In my 35 plus years of observing the market, I have learned to assess probabilities. When the probabilities are greater than 75 percent based on my indicators and the environment, I will take action. Right now, the market is in a precarious environment. It's a chronic ailment that will take time to heal and get back to a free market again.

Even with all of these warning signs, why are investors still buying stocks?

Many people are in denial. They can't believe there could be a 20 or 30 percent correction. I believe there will be a much worse correction than people realize. No one believes we could go down 30 percent, but we could. People don't want to hear about it, but it's possible.

When a bear market starts, what happens first?

When the decline starts, the S&P 500 begins to accelerate by 20 to 50 points every three days while the plus days are in single digits. For example, the S&P might fall 22 points, but rallies only 6 points. As the market turns, it falls very quickly. The rallies are labored and

slow, and on low volume. On the selloffs, the volume is much higher.

On the chart, the market is making lower lows and lower highs. You will hear people suggesting that you buy the dip, but the rallies don't come. People think it's an opportunity to buy, but it's a falling knife. Those who are up 150 percent over the last two years believe they are safe, so they hold. It will take more convincing before they are willing to sell.

What does it feel like to be in a bear market?

Bear markets can destroy people's lives, which is why you need to be prepared for them. One of my

acquaintances, an incredible human being, had gone through a series of awful events. He was on his third marriage, his son had committed suicide, and he had conquered alcoholism. He survived all of these situations. But he couldn't handle a bear market.

I was in my twenties at the time and I noticed that he had lost his confidence. He started asking me for financial advice, but I knew nothing. He couldn't see a way out of his financial problems, so he killed himself. Sadly, if he had been able to withstand another six weeks, he might have survived the financial tsunami. Markets can make you doubt yourself. He turned from a rational genius to a man with no confidence who

saw no way out.

Bear markets are destructive and destroy a lot of people. A full-blown bear market oozes downward in a slow and methodical way searching for lower levels like lava. The ooze just keeps moving down the hill, destroying everything in its path. No one is immune to the lava flow. You'd be amazed at how slow it seems, but it creeps up on you, and before you know it, you're down 10, then 15 percent.

As the market starts to fall, it starts to accelerate on the downside, and could be like an avalanche, and the entire market begins to give way. The pebbles and rocks fall with greater and greater speed and energy. Most investors think

it's a buying opportunity, but it's not. We haven't had a double-digit decline in more than two years, which is really stretching the timeline. This usually increases the extent of the decline.

What else have you learned about bear markets?

They usually last between 18 and 36 months. The worst bear markets are cancerous, and eat you up, which is how they develop. Typically, the Dow is the last to make all time highs, which is typical. In 2014, Caterpillar, Disney, and Merck were holding the Dow up. If you took those three stocks out, you would have been down for the year. In late September 2014, the Dow Industrials

made a higher all-time high on low volume. Death Knell! In December 2014, there was another rally. We saw marginally higher prices in the S&P 500 but it was a labored rally. The CCT made a lower high. That was a warning flag.

Guess what? You need a better foundation for a 100-story building. The foundation has been crumbling but you don't see anything until the building collapses. The foundation of this market has collapsed. When you add in contracting volume and excessive margin interest, it sets off alarm bells. In December 2014, we saw the Nasdaq make a lower high while the S&P 500 made a higher high, another non-

confirmation.

If the Federal Reserve were smart, they would allow a 10 percent correction and let some of the steam out. That would have been a lot healthier for the market. Instead, the market went higher. Now, instead of a healthy 10 or 20 percent correction, they could cause a 40 to 60 percent crash. After the market falls by 20 percent, there will be more concern. It starts escalating. Usually, there is an event that causes it to capitulate. One thing I learned from studying previous market crashes: The next crash is always worse than the last one.

How does a bull market usually

end?

It won't end until there is a blow-off rally that makes the prices go parabolic. At the end of 2014, the market went parabolic, which is a sign the rally couldn't be sustained. Bull markets in any market generally end with some type of blow-off that could be associated with a news item. In December 2014, the S&P futures had 38 consecutive trading days without a 30-point swing downward. It created a bubble of historic proportions, one that can only exist with extreme complacency.

Why is that so important?

The stock market must rest to recuperate and rejuvenate to mount

another rally phase. The farther the market extends without a 30-point correction, the greater the pressure becomes. That was one of the most extended short-term situations I have ever witnessed. Finally, on the 39th day, there was a 30-point correction. Because of the number of consecutive days we went without a 30-point correction, that is my definition of a parabolic move. To me, that was a line on the sand of a changing market environment.

What happens next?

Eventually, the market rolls over and goes back down. It breaks the upside momentum and changes the environment

from a rally to the start of a persistent decline, usually a 5 percent or greater correction within 60 trading days.

In the last quarter of 2014, the S&P went up over 250 points without a correction. That is astonishing. Strong bull markets go up and down like a stair step. This was more like a blow-off. The higher the market goes, the higher the probability there will be a huge decline. The market will go down a lot harder than anyone can imagine. At the top, like in 2015, no one thinks the market will go down. Unfortunately, the market could be in the dead zone for years after a major correction and bear market. When a bear market injures portfolios, it can take years to heal, if ever. Typically, the

longer a bull market continues, the longer the bear market.

What is like to be a short-seller?

It's not easy. People call you names and tease you. As the market goes higher, you feel terrible, and you lose money if you are shorting. Because the market has an upside bias, people treat you poorly, and they don't want to listen if you try to warn them. It takes a long time to get vindicated because it often takes a long time for the market to top out. It takes even longer for people's perceptions to change.

What do you look for when the market is collapsing?

I look for the speed of the movement, which increases volume, volatility, and therefore, opportunity. You can make more money in bear markets because the market goes down three times faster. It goes down quicker and is more liquid. It's similar to being in a smoke-filled room that is ready to burn up and you don't know where to go. You have to know where and when to exit. A collapse creates speed, frenzy, panic, and chaos. Each of these circumstances reduces a person's ability to act rationally.

How bad can it get?

I don't think people have any idea.

We are in what I call an ominous

environment. The thunderstorm is approaching and we know it's coming. All of the characteristics are there, but the severity of it is the big question mark. You also don't know when it's going to hit. When you see a storm looming, you go into the basement. Right now, I can sense that something isn't right. I can feel it.

The majority can be right for a period of time but eventually the purging comes. Purging means to change or eradicate excesses that create unhealthy, obese prices. Around the world, different market environments have experienced this obesity. A person who is 300 pounds overweight will take a considerably longer time to lose pounds

than someone who is 50 pounds overweight.

Therefore, a bear market will be present for a longer time period if the previous bull market was an elongated, protracted aberration that didn't purge itself with a correction. The stock market is on a non-stop Twinkie binge right now. It's gone two years without a double-digit percent decline. In medical terms, the stock market has clogged arteries, high blood pressure, reduced mobility, and less energy.

Can you make money in a bear market?

Absolutely. First, once the correction starts, only traders will make money. As

the market starts to plunge, the volatility will be incredible. The rallies are tepid and labored, while the selloffs are sharp and hard. The selloffs are three times faster than the rallies.

Can you take me through the different stages that a bear market goes through?

This will be a long answer, but based on my experience, here are the different factors that form a bear market. First, it takes a long time for investors to change from overconfidence to fear, especially if the bull market lasts as long as five years.

STAGE 1: The first factor I observe are the rallies. If the market does not

rally strongly and even better, if it cannot hold its gains, this is a clue the market is wounded. It will be vulnerable to further injury if there are lower lows on the chart.

STAGE 2: I am suspicious if there is a lifeless rally in a low-volume environment. This tells me the institutions are not willing to buy. Since institutions are generally a herd and they watch their peers closely, if the entire pack doesn't follow in lockstep immediately, the rally falters. You will hear people say, "This time is different, and history won't repeat itself." But history always repeats itself. One of my rules is to study past history so you aren't doomed to repeat those

consequences unprepared.

If there is a market rally, I will also look at the NYSE Tick and see if there are plus tick readings as high as plus 1000. If I get those readings, it tells me the rally is genuine. On the other hand, if there is a double-digit rally, but we don't register 1000 plus ticks, then the rally is suspect.

You should know that in the fourth quarter of 2014, we were stuck in Stage 2. Even more interesting, the daily CCT readings I was recording showed that we were already in a bear market. In other words, although the market was slowly moving higher, the tick was giving me unenthusiastic NYSE Tick prints that were barely positive. That

divergence was a huge red flag. Actually, the divergence was almost as wide as the Grand Canyon, which is why I'm so confident the bull market's days are numbered.

STAGE 3: The rallies are tepid and weak, have no energy, and are very negative. That's how bear markets start. It usually starts off slow and goes faster and faster like rolling down a hill, and then you have an avalanche. You may then lose 50 or 60 points on the S&P 500.

After a greater than 3 percent correction, the market should be able to mount a meaningful reflex move. If not, then that is a red flag. For example, if there is a 4 percent correction, but the

market is unable to bounce back at least a half (or 2 percent in this example), the bear market has arrived.

I also look at the speed of the bounce. In a mature bull market, the market will be unable to bounce back quickly or with any zeal. If it cannot bounce back (retrace) at least half of the bounce, that's a red flag. The bear market is here!

We entered stage 3 in December 2014. Then the daily CCT was unable to make a higher high while prices did. Then we had a blow-off rally as the tepid market made one last gasp rally attempt. We rallied 250 points on the S&P without a correction of even 30 points. When you look at the chart, it

was going straight up for two months. That can't be sustained. The 30-point correction came in early December 2014. This marked a change in the environment as the euphoria ended. Nevertheless, complacency was still as great as ever.

STAGE 4: I also look at what the charts are telling me. A lower low on a chart tells technicians that the mood of the once invincible market is vulnerable. Technicians who study charts believe that if the market closes with lower lows, buyers will start leaving. Therefore, the first clue comes from the chart, and technicians are often the first to see that the first pullback is severe.

The stubborn bulls hold their position

while sweat beads appear on their brow. They say to themselves, “I can’t sell here.” The longer they are in the black (profitable), the more staying power they have.

STAGE 5: During this stage, the market begins to accelerate to the downside by eroding 20 to 50 S&P points every three days, while on the plus days, the market only goes up by single digit S&P points. The move downward occurs quicker while the rallies are labored and slow. At this stage, bulls are still buying on the dips, but not as enthusiastically. Therefore, the volume during declines is increasing while the rallies are not as energetic. Nevertheless, most bulls are not thinking

of selling. It will take a little more convincing before they reach the selling stage (usually when it's too late).

STAGE 6: On the chart, the market makes a lower low for the entire quarter or hits a double-digit correction. You will see a stair step of lower highs and lower lows that persists. Volume will increase but has not spiked yet. Time has become an enemy of the bulls.

Now that portfolios are down by 15 or 20 percent, bullish investors are thinking of selling. A double-digit decline causes huge redemptions. Even money managers are thinking of selling as redemptions hit. Double-digit declines trigger more mutual fund redemptions.

STAGE 7: Institutions are starting to lighten positions because they fear investor withdrawals. The negative quarter irritates investors, which is the first hint their mood is changing. Eventually, they will move from complacent peacefulness to terrified panic, but that takes time. Stubborn bulls have not liquidated their positions, but investors are buying less. Eventually, the market will give up all of its previous gains.

STAGE 8: The news is becoming more of a factor. As the bear market picks up steam, there is less good news. Economic releases are now viewed with more skepticism. Analysts are concentrating on less stellar numbers

while ignoring good news as inaccurate or suspicious. The scale is now tipping towards terrifying panic, but stubborn bulls still hold their positions even though sweat beads become torrents.

STAGE 9: Volume increases almost daily with consecutive down days. A rally lasts one to three days, while declines might last as long as 5 to 10 days. The stubborn bulls are starting to liquidate. After they are down 20 percent, they think the worst is over. Many people think that the Fed will save them like they did in the past.

When the market keeps falling, that's when the institutions get out. They are forced to get out because of the redemptions. At this stage, the Fed is

ignored and their credibility is lost.

STAGE 10: The financial news networks parade the bears on TV while the bulls are viewed as frauds. Most bulls go into hiding and don't want to appear on TV. They are busy trying to calm their clients! The official bear market is here, having eroded more than 20 percent from the highs. The bears add to their positions, while the word, "complacency," has long been a fleeting thought of investors. Any bad news gains front page attention on all the networks. The bulls liquidate more as red ink has replaced what were gains only months earlier. Waves of minus 1000 ticks are registered. Volatility increases each day as double-digit down days are more

prevalent. The market crosses the 30 percent correction level with a straight line down.

STAGE 11: This is when the bulls capitulate. After they look at their statements, people panic. They grasp on the hope the Fed will help get their portfolios back to even. And once they realize they won't, they panic and sell. That is when investors throw in the towel. Volume will be at greater than three times normal. Instead of one million S&P option contracts, four million are traded in one day. At this point, the market is overheating, and it will blow a gasket. The NYSE Tick readings will register multiple readings between minus 1600 to minus 2100.

Financial firms are on the brink of collapse, and more firms are in trouble. No bull will ever admit they were bullish as they liquidate nearly all of their positions, turning once profitable portfolios into a sea of blood. It's an avalanche of selling. Many brokerage statements reveal equity losses of 50 percent or greater. Also, investors will ignore margin calls. In addition, there will be one-day downward moves that exceed 100 S&P 500 index points.

Investors lose all confidence while brokerage firms liquidate investor portfolios that are heavily on margin. The market goes from being the belle of the ball to the ugly sister. The market is hated, and investors cry in despair, "I

never want to be in the stock market again!” Two full years of gains eliminated in months. There won’t be anything viewed as safe as all asset classes fall together.

What strategies should investors use in a bear market?

I have made the most money in bear markets but it’s not easy. Some of the strategies I have used include buying puts on the S&P 500, buying inverse ETFs, shorting individual stocks, and most importantly, sell long positions and move into cash until the storm has passed.

If you decide to buy puts either for speculation or protection, I strongly

recommend buying Michael Sincere's book, *Understanding Options 2E* (McGraw-Hill). His book covers both basic and intermediate strategies.

Since most people aren't day traders and have difficulty managing short positions, moving into cash is the most prudent strategy. If you wish to remain long a few stocks, sell down to a comfortable size. Investors must ask themselves: How much pain can you stand? Over the next couple of years we should see a 30 percent correction in the stock market. If that is tolerable, then stay the course. If not, then move to the sidelines.

What happens when people gets

themselves in trouble in a bear market?

I would recommend that they understand volatility. Buy and holders want to hear that they will be all right during a bear market. They are basically going through the five stages of grief: denial, anger, bargaining, depression, and finally acceptance. Once you get to the anger stage, you have a chance to do something about it. The market will give you enough volatility to get you out of your mess. You need to have a systematic plan. I tell those in the anger stage they must get smaller. If you're 100 percent invested, take 20 percent off the table. With every rally, take off 20 percent. They usually won't do it until

they are forced to.

I know that you are primarily a trader rather than an investor. For those who want to trade, what are the characteristics of a successful trader?

The first characteristic is tenacity. A successful trader is focused like a laser beam with a goal to build greater assets each day within a reasonable timetable. Everyone wants to make a million dollars in one day, but a successful trader is realistic about what he or she can achieve.

In addition, a successful trader must be willing to commit to it full time. If it is a hobby or not taken seriously, the end result will be a big minus sign. Trading

must be considered a profession, and if not, then you will be separated from your money very quickly.

Also, your trading habits must fit your personality. If you are an impulsive individual, your style will reflect your trading strategies. On the other hand, a calculating trader will wait for all the indicators to fall into place before making a trade. Your personality will determine your success or failure more than any other factor.

For example, if you are greedy or fearful, that will affect your trading decisions, and more than likely, you will be wrong. Whenever I feel the most greedy and have “walk-on-wateritis,” and feel I’m invincible, I must short this

market. I feel that the vast majority of the world's investors feel they are invincible to any correction, which is the ultimate complacency. When you start to feel invincible, watch out. You will go down like the Titanic. Discipline must win out or you are doomed to failure.

Finally, the primary mindset must be survival. Unfortunately, most people experience a mortal wound before they have acquired the necessary survival skills.

Is there something else successful traders must do?

Yes. They must know themselves. Experienced traders can objectively list their strengths and weaknesses. If you

cannot be true to yourself, you will never be true to anyone. Trading allows transparency to the soul. The market will ferret out your weaknesses by seducing you into dangerous environments. The greatest disease that is always terminal is greed. That glaring sin is damning to an amateur trader. I have warned many aspiring traders that losing builds character, while greed destroys it.

What is one of your most important rules?

The reason that I have survived as a trader so long is that I have an important credo: There is always a way to make money, and it's a trader's job to find it. I've been through some difficult trading

environments but I am determined to survive and thrive. The truth is that when I follow my business plan, suppress emotions, eradicate greed, and minimize stubbornness, prosperity follows.

This may not come as a surprise but I love bear market environments because volatility increases. I make the majority of my money in adverse situations. That is where you can make the greatest wealth. In the current environment, you must be ready to take a 180-degree turn. Right now, it's like we are going through a jungle that suddenly turns into a desert. That's what could happen.

I made my first million dollars in 1987. I cleaned up in 2000. And in 2008, a double-digit percent gain was

recorded. With over 35 years of trading experience, I have seen this story before. The names and dates have changed but the story is the same. I believe that 2015 and beyond will be rough for the market, but good for traders.

What are the biggest mistakes that new traders make?

First, before you start trading, you must deflate your ego so that you allow yourself to learn. Another stumbling block is laziness. There are no shortcuts in trading. Hard work in trading translates into greater success. The harder you work the better you will be paid.

Do you have other suggestions to help traders?

A business investment plan is an absolute must. The plan covers many specifics including the best markets to trade, a profit objective, and risk management with step-by-step instructions. The risk management section also includes different scenarios that will help you no matter what the market environment. Missing steps is similar to a trapeze artist with a misplaced or nonexistent net. One slip and it is death. Also, a business plan has a big picture approach to the market. And finally, traders must be aware of their personalities, which will help them determine what strategies to use.

Why is a business plan so important?

A good business plan gives you confidence that you are on the right track. Otherwise, you are playing it by ear, which is a disaster. When you don't have a plan, you tend to rely on your emotions, which will cause mistakes, especially with entries and exits. The goal is to enhance your strengths while minimizing your weaknesses. With a business plan, you are less emotional about trading, which allows you to focus on the facts rather than fear or greed. Being prepared is the key, which is why a business plan is essential.

Has a business plan helped you?

Absolutely. One of the reasons I won the 1992 U.S. Investing Championship was because of my business plan. I garnered a 563 percent return that year, minimized losses while maximizing profitable opportunities. And all of it was outlined in the business plan. Now, I don't trade without a plan. It helps gives me a big confidence boost which translates into hard dollars.

How much profit should a trader expect to make?

There is a reasonable amount of profit that is available in every trading environment. Expecting too much profit unleashes greed. If investors think in their mind they should achieve a pre-set

amount of profit, and accepting it graciously, they are maturing as a trader. Immaturity is obvious when they believe the profit objective was reached, and it was not enough! The more you want, the less you will receive. The profit objective was reached, yet the person's emotions allowed greed to ask for unreasonable expectations.

How can traders suppress the urge to be greedy?

The first trade that traders make helps determine how they will handle future profits. When I meet first-time traders, I tell them, "I hope you lose." The response I get is very revealing. If they are angry or resentful, that person has a

stubborn streak that will be their Achilles heel. If they are confused, and reply, "Why do you say that?" then the trader might be willing to accept criticism, and have a trading career. A rational mind realizes probabilities and lives by them. A lottery ticket buyer mentality is not dealing with probabilities. Many small gains are possible and probable. Live with that truth and greed will subside.

What's a common mistake that traders make?

A very common mistake is investors are overexposed to equities when markets are calm. Then when volatility increases, they are unwilling to

participate. I have seen investors become complacent, unconcerned about being overly exposed. I have heard countless traders say, "I will react when I should." Instead they become frozen with fear and fail to react at all. The investment position turns against them. They do not use hard stops, which is a recipe for disaster.

How hard is it to be a trader?

It's very hard. The work ethic cannot be overstated. I watch the market all day long from the opening bell to the closing bell. I have kept diaries every day in the market for the last 30 years, sometimes with 40 entries per day. If I do not make entries in my diary, my work suffers.

There is no short cut in trading. The market will quickly find out if you are lazy.

How do you prepare for a trade?

You prepare by creating a trading plan. Start by planning the worst-case scenario and work from there. You are never more objective than before you execute a trade. Once you are in a trade, your emotions take over, so the plan must be in place before any activity takes place. When you have a plan, it will help tell you when you are wrong. You admit it, get out, and retreat. Live to fight another day. Retreating is a cowardly approach but it will keep you from a trader's obituary. I have been

diagnosed as terminal many times, and rehabilitation takes time, but it's better than death, which is final. One more piece of advice: Never allow a 50 percent loss on a position, whether a trader or investor. Exit before you lose 50 percent. A comeback from a 50 percent loss to break even requires a 100 percent move, which is highly unlikely. Turn your weaknesses into strengths.

How do you turn weaknesses into strengths?

Experienced traders know their weaknesses. You have to know where you're vulnerable. For example, I'm vulnerable to news items, so I don't

trade on breaking news. It means understanding yourself as a person and a trader, and keeping a journal of your mistakes. Remember that it's okay to make mistakes and have weaknesses, but don't keep making the same mistakes over and over again. That takes experience and discipline.

I can tell you really love being a trader.

To me, trading is a dream job. First, you can live and trade anywhere in the world. I call this location independence. Second, you only have one boss and that is yourself. It teaches you to believe in yourself, which is the ultimate responsibility. Traders don't have the

luxury of relying on others to bail them out or to take the blame for poor financial decisions.

However, you will receive your just reward when you work hard and make correct decisions. No one will steal your limelight or take credit from you. You are the boss of your past, present, and future. You get to answer only to yourself, not to someone who you don't respect or like. This is boss independence.

Finally, trading has no salary restrictions. Literally, your earnings potential is infinite. The decades I have traded have provided me with more income than I could have made in any other profession. The market is the only

restriction to the amount of money to be made. This is financial independence. I needed something that would challenge me every day, and trading did that for me. It took me a long time to figure it out.

Should traders get help from others?

Definitely. Would you consider climbing Mt. Everest without a guide and totally alone? Absolutely not! Unfortunately, many people don't search for a trading mentor, or even observe those who are successful. Often, ego is the greatest barrier. Inexperienced traders believe they can start making money without taking the time to practice

or even learn the rules.

Everyone who trades will experience a period of angst. This environment will start slowly or abruptly change. These changes can end careers if unknown to the trader. This uncertainty also causes traders to make impulsive decisions that turn out to be wrong. A mentor helps provide counsel and comfort and help calm nerves by providing insights or help in assessing probabilities. A good mentor can help suggest a route that will bring the trader back to financial health. They will help traders navigate through treacherous mine fields.

Any final thoughts?

My grandfather said to me, “If you buy

what no one wants, and sell what everyone wants, you will never go bankrupt.” These words, which I ponder almost daily, should be the motto of every trader and investor. That simple approach has guided me throughout my career, but it took years for me to understand. I also learned that the more people who have the same opinion, the greater the probability the opinion is wrong.

Unfortunately, only a small minority of people will be prepared to withstand the typhoon of asset destruction. Even fewer will actually prosper. The bubble of 2015 will be a historical Armageddon. History will view 2015 and beyond as an era of excesses that were

unsustainable. When the bubble bursts, a Pandora's box of horrors will be released. I say this not to create a panic, but to save financial lives.

Conclusion

by Michael Sincere

Mark Cook has witnessed several bear markets in his career. Mark not only survived these environments but also profitably traded during the collapses of 1987, 2000 and 2007. In all three, investors who held on to their long positions as the bear markets unfolded saw their portfolios get crushed.

Most investors were unable to heed the warning signs and get out before share prices plunged. Many simply held on until the bloodbath was nearly over. Then they finally surrendered and sold at

or near the bottom of the crash.

Mark and I wrote this book to help you avoid making these costly mistakes. Hopefully, reading the interview with Mark has enabled you to understand the warning signs that a bear market is imminent. Mark is confident that these signs have become more and more clear.

You may be wondering what you should do now.

1. First, you can disregard Mark's warnings and hold on to your long portfolio. The risk is that if Mark is right, your portfolio could decline by 20 – 30 percent or more. Are you comfortable taking that gamble?

2. If you are unconvinced by Mark's analysis and remain bullish, you could keep buying stocks. Should the bull market continue, you will be very glad that you disregarded his warnings. However, if Mark is right, your losses will be even greater than those who simply held their long positions.

3. If you find Mark's analysis to be persuasive, the wise thing to do is seriously consider selling much or all your stocks to lock in your profits. If you have specific positions where you have paper losses of more than 10 percent, you might want to close out your positions before your losses mount.

If you do sell some or all of your stocks too soon, you risk the ridicule of your friends and colleagues. Can you handle that? Think about those investors who did sell early during those last three major crashes. They probably had the last laugh.

4. The final choice is to sell your long positions and attempt to profit from the bear market plunge. This would require another book to discuss in detail (one suggestion is to read my book, *Understanding Stocks 2E*), but here are other ideas: You may sell short (only for experienced traders), buy non-leveraged inverse ETFs, or buy put options. Keep in mind that if you do use any of these

strategies, you must take profits quickly. Because bear markets are so volatile, few investors make it to the Winner's Circle. Now that you have read this book, you will be better prepared.

Finally, I want to applaud you for purchasing this book. It is my hope that it will help protect you from what we think is an imminent financial bloodbath. Good luck, and feel free to write me at msincere@gmail.com if you have any questions. I look forward to hearing from you.

Author Biographies

Mark D. Cook

Mark D. Cook is a professional trader. In 1986, he discovered the Cook Cumulative Tick (CCT), which helped him profit from the 1987 market crash and also rise to fame in 1992, when he won the U.S. Investment Championship with a 563 percent audited annual return. It was the highest percentage in all investment categories. In 1993, he followed up with a 322 percent audited return in the U.S. Investment Championship.

From 1992 until 1996, he was a commentator in *Barron's* financial magazine, writing about options. Forbes Magazine profiled Cook in a 1994 feature story on his trading strategies. Cook has also been profiled in investment magazines in Russia and Australia, *Stocks and Commodities* magazine, *Futures* magazine, the *Wall Street Journal*, and *SFO* magazine. He has also appeared on numerous financial programs including Fox Business News. He also writes articles for MarketWatch.

Cook was also included in the best-selling book by Jack Schwager, *Stock Market Wizards*. He was selected after Schwager reviewed his audited nine-year performance track record. Cook

was the only wizard who primarily traded S&P 500 index futures.

In 2001, Cook was featured on the cover of *Active Trader* magazine. He has also been included in the following books: *Psychology of Trading* by Russell Wasendorf, *Extraordinary Comebacks* by John A. Sarkett, *Pit Bull* by Martin “Buzzy” Schwartz, *The Long-Term Day Trader* by Deron Wagner and Michael Sincere, *Inside the Investor’s Brain* by Dr. Richard Peterson, and *When Super Traders Meet Kryptonite* by Art Collins.

Cook has privately mentored and instructed thousands of students over the last 20 years, helping them to become professional traders. He has authored the

Cook Investment Advisory letter, a twice-daily e-mail that is circulated world wide. Mark has spoken throughout the world including China, Australia, Mexico, Canada, Bahamas, and Singapore as well as years of presentations in the United States. He currently welcomes any and all speaking engagements to educate people on how to trade in all environments as a career.

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Michael Sincere

Michael Sincere is the author of a number of investment and trading books. As a financial journalist, Sincere has written hundreds of columns and

magazine articles on investing and trading, including a monthly column for MarketWatch.com. He has been interviewed on dozens of national radio programs and has appeared on several financial news programs, such as CNBC and ABC's World News Now, to talk about his books.

He is the author of the best-selling *Understanding Options 2E* (McGraw-Hill), *Understanding Stocks 2E* (McGraw-Hill), *All About Market Indicators* (McGraw-Hill), *Start Day Trading Now* (Adams Media), and *Predict the Next Bull or Bear Market and Win* (Adams Media).

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